

The **consumption function** (A.1) arises from the maximisation problem for individuals

It expresses desired total consumption of non-durable goods ( $c$ ) as a simple linear function of wealth, given preferences for other expenditures that yield utility, such as dwellings and money.

$$c_t = \frac{mpc_t \text{wealth}_t}{pc_t} \quad (\text{A.1})$$

Equation (A.2) is the **marginal propensity to consume** out of wealth ( $mpc$ ), which is derived from the first order conditions of households. For compactness it is expressed as a forward difference equation, but can also be expressed as a function of the discounted sum of present and future interest rates ( $rg$ ), consumption prices ( $pc$ ), the user cost of dwellings ( $duser$ ), as well as the structural preference parameters for households' discount factor ( $\beta$ ), expected survival rate ( $\gamma$ ), the elasticity of intertemporal substitution ( $\sigma^c$ ), and the weight on real money balances in utility ( $\psi^{mon}$ ).

$$\begin{aligned} mpc_t^{-1} = & 1 + \frac{duser_t \zeta_t^d}{pc_t} + \frac{(\zeta_t^{mon})^{-\sigma^c}}{\psi^{mon}} \left(1 - \frac{\gamma}{1 + rg_t}\right)^{1-\sigma^c} \\ & + mpc_{t+1}^{-1} \gamma \left[ \beta \frac{\zeta_{t+1}^{mon}}{\zeta_t^{mon}} (1 + \dot{y}_{t+1})^{\psi^{hab} \frac{1-g^c}{\sigma^c}} \right]^{\sigma^c} \left[ \frac{pc_t}{pc_{t+1}} \frac{1 + rg_t}{1 + \dot{p}_{t+1}} \right]^{(\sigma^c-1)} \end{aligned} \quad (\text{A.2})$$